Big Bang—A Retrospective

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BOOK REVIEWS

Crash Bang Wallop: The Inside Story of London's Big Bang and a Financial Revolution that Changed the World by Iain Martin, *Sceptre, 2016; pp 340 + x, ₹599/UK£14.99.*

Peppered with anecdotes and written in a racy style, the book on the conjunction of events and circumstances that transformed the character of the City of London as an international financial centre is a delight to read. Till the day of the Big Bang on 27 October 1986, hailed by many as a "cosmological event," the institutions in the City operated like private clubs, each under the effective control of a family managing the money and affairs of at most 500 well-connected British families. The mid-1960s witnessed major stirrings. London became the centre of euro–dollar bond market, thanks to a brilliant innovation by Seigmund Warburg, the German Jewish banker, a somewhat late entrant to the City. Hordes of American investment bankers and Japanese bankers descended on London given its geographical positioning to act as a bridge between different financial centres across the world.

On May Day 1975, sweeping changes in the working of financial markets revolutionised Wall Street in New York but this did not shake either the City or the Government of the United Kingdom (UK). The brokers and jobbers who were sheltered as part of a protective cartel and were prisoners to their own insular beliefs and interests, remained pleased with the continuity. The government seemed reluctant to take the initiative for reform, deeply preoccupied as it was during the 1970s with its own financial difficulties and in securing a lifeline from the International Monetary Fund. In any case, the government's attitude was, by and large, the same as it was in the heydays of British dominance. The City claimed to know what was best; and if those who were the key players in the City were reluctant to let in fresh air by way of competition, it was their business or so it was believed.

How did the ambience change? What kind of forces propelled it? This is the main burden of the book. The effective trigger for the transformation was the full-scale abolition of exchange control, a complete break from the collectivist attitude followed since World War II—a decision taken in desperation to rescue Britain from dire economic distress. Geoffrey Howe, Chancellor of the Exchequer, announced in Parliament on 24 October 1979:

> There will from tomorrow be full freedom to buy, retain and use foreign currency for travel, gifts and loans to non-residents, buying properties overseas and investment in all foreign currency securities... Portfolio investment will be wholly freed and the requirement to deposit foreign currency securities with an authorised depository is abolished. Foreign currency accounts can be held here or abroad. Passport marking for foreign funds can now be abolished. (p 99)

Characterised by opponents of the Labour Party as a "reckless, precipitate, doctrinaire" decision, it nonetheless led to a huge inflow of money with flows of foreign investment going up very significantly. The situation was reminiscent of the bold British switch to free trade in the mid-19th century. By itself, exchange liberalisation could have revolutionised the financial market if the stock exchange was prepared to change the way it used to function: doing away with its restrictive membership, fixed commissions and antiquated practices. But those who ran the exchange were adamant. They preferred, instead, to lobby persistently with the British government for securing an exemption from the jurisdiction of the Restrictive Practices Court to which its rule book stood referred to by the Office of Fair Trading. Understandably, the government was not prepared to interfere with the legal process. However, at the same time, it chose to wash its hands off and let the status quo prevail although this was clearly not in the larger national interest.

Muddling Through

This stalemate needed to be broken. If the legal case went ahead, the City would tie itself up in countless knots and endless litigation causing irreparable damage to London's reputation as a financial centre. It was the Bank of England that then took the initiative to break the deadlock. It could not afford to sleep over its concern over the functioning of the securities market for which it was responsible: the City's firms that were grossly undercapitalised had to be reformed in order to have adequate clout in a market that was more competitive. Given the fact that the Bank of England had no formal powers to intervene in the stock market and that exchange itself was supposed to be a self-regulating organisation, the bank embarked on the only course open to it: initiating a dialogue among officials representing different interest groups in the stock exchange, the Treasury and other departments of the government. After four years of secret negotiations, bank officials were able to give shape to the terms of settlement and avoid getting bogged down into a quagmire of litigation between the Ministry of Trade and Industry and the stock exchange authorities.

When the settlement was announced by Margaret Thatcher soon after her landslide victory in 1983, there was a big public outcry: Why was the government skirting round the Restrictive Practices Court? The *Economist* spoke of "the Square Mile having been done a favour by its chums." Even a Tory friendly MP said in Parliament,

> Is the Secretary of State asking the House to accept that the deal between the cronies in a smoke-filled room is a substitute for a full public inquiry into how public interest is

affected by a major institution such as the Stock Exchange? (p 106)

Another hurdle had to be crossed. There was little clarity as to the kind of regulation that had to be put in place. The City, as expected, was in favour of minimal regulation in tune with the impressive motto it had been always proud of: "My Word is My Bond." The Labour Party was in favour of comprehensive regulation. Should there be a tough and independent Securities and Exchange Commission modelled on the United States institution? Or, as many argued, should re-regulation be limited to general responsibilities for oversight? But then the question arose as to under whom there would be oversight. There were several contenders from within different departments of the government and the Bank of England.

As the Big Bang neared, it started dawning on the government that with the change in the character of the inflows coming into the stock exchange, notably foreign finance, as well as the new institutions, it was essential that the competing claims being made of financiers, the stock exchange, the foreign players in the Euro-bond market, the Bank of England and the Treasury be reconciled in the form of a tough, coherent and workable piece of legislation. The Financial Services Act of 1986 formalised regulation while safeguarding enough of the City's independence and accommodating the interests of diverse groups.

Role of Individuals

The process of resolution was a classic instance of "muddling through." A good many books have been written on this period. The fourth volume of David Kynaston's book *The City of London: A Club No More, 1945–2000* covers the period comprehensively. What gives Martin's book a distinctive flavour is a blow-by-blow account of the events that took place and the specific roles played by a wide range of personalities who had stakes in the reforms process. Though none of them had a clear idea of the final outcome, they succeeded in breaking the ice among themselves through a process of intense and continuous dialogue.

Positioning himself somewhat as an anchor person, the author digs up colourful actors from elite establishments and recreates the turbulent 1980s. Nicholas Goodison, chairman of the stock exchange, a hard core conservative immersed in the study of furniture, clocks and music, and wedded to the "club mentality," ironically becomes the driver of reform. How this change in temperament and outlook comes about has been interestingly captured. George Hayter, charged with the task of creating a new electronic marketplace, finds his task easier than overcoming the "sniggering cynicism" of many traders. The historic 1983 settlement between the stock exchange and the British government's Department of Trade and Industry (DTI) was the silent and secret handiwork of a few dedicated individuals. To David Walker, executive director of the Bank of England, goes the credit of setting the ball rolling, putting the game-changing paper by the young economist Andrew Threadgold on the table of the Prime Minister in Downing Street. Of the roles played by many other confidantes of Thatcher, among whom Arthur Cockfield deserves a special mention and who later became Commissioner of the European Union (EU), he worked on the preparation of the Single European Act of 1986 that made it possible for the City to become the undisputed financial capital of Europe. No less important was the role played by Michael Howard, parliamentary under secretary at the DTI, who fumbled initially in seeking to grasp the intricacies of how a financial market works, but who could ultimately hammer out a piece of legislation that struck a balance between political realities and the accountability of market players.

Along with the events, chaotic at times, the author captures the cultural life of the City: theatre, music, fashion and satire. And he has not missed out its unique and enduring quality—its pride on the patch of ground on which it had been doing business for centuries.

Consequences

As competition was unleased, the British-owned large clearing banks and major merchant banks made ambitious moves to own and operate investment banks on a global scale. However, the cracks in their

edifices surfaced much sooner than what could be imagined. The American banks were waiting for the opportune moment, and with their resources and the skills they had acquired over the 1970s in managing the highly integrated and complex business of broking, market making and corporate advisory services, they grasped it when it came. Even Continental Europe, with scarcely an equities culture let alone an interest in investment banking, shot into the limelight.

The resources of the British-owned investment banks were not as massive as those of the American counterparts, and added to it was their shoddy, arrogant and amateur managerial culture. The symbol of British power and dominance stood completely humbled. The City turned into a branch office of New York, belying the expectation of the government in 1983 that the stock exchange and the majority of British institutions would remain in British hands—a sentiment echoed by the governor of the Bank of England. However, when the British-owned investment banks were being sold and went out of existence, the government and the Bank of England stood aside. The speed and totality of the submission of the City's leading firms stands out from the author's narration as one of the most abject surrenders in business history.

Perhaps the authorities were not convinced of any rationale for keeping any national champion; if they had, they could perhaps have intervened earlier, interacting with the leading British institutions at the preparatory stage, helping and advising them to keep on course. Do national champions have any role to play in a global financial market? Often this issue does come up in the emerging markets undergoing reforms. Arguably, in hours of distress and emergency, national champions do have a critical role to play; to strive for retaining or developing them is not blind economic nationalism, nor is it protectionism or an alternative to competition.

Perspective

As the author asserts, he has a pro-market outlook, endorsing that

> …open capital markets are a boon to humanity, matching capital with ideas for business expansion, innovation or infrastructure. The attempt to live without them to varying extents, to the first World War until the abolition of exchange controls by Geoffrey Howe and Nigel Lawson were a disaster.

But now, 30 years after the Big Bang, what kind of future do we foresee?

Over the decades since the early 1970s, in the wake of the breakdown of the Bretton Woods agreement, financial capitalism has been on ascendance. There has been an unprecedented expansion of financial activities, rapid growth of financial profits, permeation of economy and society by financial relations, and domination of economic policy by the concerns of the financial sector. The City of London, post-Big Bang, had a significant role to play in the triumph of global financial capitalism. The launch of the single currency in Europe, coupled with the continuing advantages of London in terms of language, time zone and culture, propelled the City to new heights.

Associated with this expansionary phase, in which New York and London collaborated frenetically, speculative

excesses and reckless greed displayed by the market players almost blew up the global financial system in 2008. Much of what happened is not really new. It has been all there, in one form or another, in the history of finance. The key differences are the huge scale and complex global links of financial activities. Severe social and economic disruptions in the wake of the crisis have generated disillusion among less affluent ordinary citizens about the benefits that accrue from liberalised financial markets. Brexit is the visible expression of that underlying concern. The UK has chosen to leave the EU. Cut off from Europe, will the City be able to retain its dominance in the global financial market?

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